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SUBJECT: AMBASSADOR'S MEETING WITH DPM BARHAM SALIH ON
HYDROCARBON LAW

Classified By: AMBASSADOR ZALMAY KHALILZAD, REASONS 1.5 (B) (D)

11. (S)Summary: Ambassador met January 23 and again on the 24th with DPM Barham Salih to seek a way to get the Hydrocarbon Law process back on track. The latter meeting included Minister of Oil Shahrستاني, the PM,s Oil Adviser, Thamir Ghadhban, and, briefly, other members of the Energy Committee. The outstanding issues seem to be reduced to two: the management of disputed territories, resources under the Art. 140 process of the constitution; and, more significantly, the continuing dispute between the KRG and the central government over the powers of the Federal Committee on Oil and Gas to approve regional contracts. The DPM plans - at the Ambassador,s request - to resolve all outstanding minor issues and present a clean text with bracketed language on the two points in dispute. Barham expressed optimism that this should be possible in the next day or two. The step after that will be to use all powers of persuasion to bring the KRG leadership on board with a formulation that is sufficiently unambiguous with respect to approval of contracts that the draft law will not be fundamentally weakened. End summary.

12. (S)The Ambassador met on the evening of Jan. 23 with Barham Salih to discuss the breakdown in CoR efforts to approve the ,07 budget and the state of play on the Hydrocarbon Law (HC). The DPM said that on the surface, the main budget issue was Kurdish insistence that there be a separate budget line for the Peshmerga in the 2007 budget for their deployment for national security goals. He also added that there was disunity among the Shia groups in the United Iraqi Alliance (UIA) but that he expected the budget to be passed perhaps next week. On the HC law, he explained that Oil Minister Shahrستاني recognized that he had gone too far in his revised draft of Jan. 19, even apologizing to the Energy Committee at its session on Jan. 22 for proposing changes in the draft text that had not been discussed in any previous sessions. Barham said that basically the committee was back to working on the December 17 draft, but that disagreement continued to revolve around the issue of how to formulate the Federal Council on Oil and Gas,s (FCOG) role in approving contracts, e.g., non-objection versus other formulations that implied a right of approval by a central government organ over contracts negotiated primarily by the KRG. The DPM also said that the details of the revenue distribution mechanism remained in dispute, with the KRG insisting that there should be a Kurdish representative within the structure of revenue collections and distribution, just as there should be among the positions that controlled the HC regime - the Ministry of Oil, the FCOG chair, and the head of INOC. The KRG was looking for balancing language for these positions. The DPM noted that one way out of the impasse on revenue was to postpone a decision on this part of the HC framework law for the time being since the ,07 budget

parameters were already established. The details of revenue distribution could be worked out in subsequent language that would cover revenues in the ,08 budget.

13. (S)The Ambassador noted that it would be difficult to find balancing language for various positions at this stage and cautioned against trying to divide up positions on ethnic or sectarian lines. He did offer to do whatever the U.S. could to break the impasse, either by providing additional drafting suggestions or meeting with the parties. Barham responded that he agreed that balancing language would be tricky. He said that at this point it was less a question of drafting suggestions than a basic decision about how to capture the relationship between the central government and the KRG, and appreciated the Ambassador's offer to use his good offices to bring about a compromise.

14. (S)Against this backdrop, the Ambassador joined the Energy Committee at the end of its deliberations on the evening of Jan. 24. Both Shahrستاني and Ghadhban had canceled their plans to attend the Davos World Economic Forum in favor of trying to work through the remaining difficulties, and informed the Ambassador that only "one and a half" issues remained - the half issue of the status of disputed territories under Art. 140, on which they were confident the KRG would compromise in favor of the central government, and on the core issue of whether the FCOG had approval rights for contracts. Barham argued that since the process for negotiating contracts - involving both central and regional elements - was spelled out so clearly, the issue of FCOG approval should not be a major hindrance. Either a formula of concurrence or non-objection should be sufficient. Shahrستاني agreed the contracting process was sufficiently iron-clad that final approval should not be a major

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consideration, but he argued strongly that it would be a major mistake to leave ambiguities in the law about the authority of the FCOG. How would the FCOG treat contracts in the future negotiated for example by Basrah, Iraq's major producing governorate? Clearly, ambiguity would not be good and would open the door to legal challenges. Ghadhban agreed, adding that any ambiguities would be exploited by MP,s from southern regions when the draft law comes before the CoR.

15. (S)The Ambassador reiterated his offer to try to help reach agreement by speaking directly with senior KRG officials. The principal members of the Energy Committee agreed to resolve any remaining minor issues in the draft HC law and present it to the key players in the next days so that a final effort to reach a final agreement can be mounted. There is a possibility that Nechirvan Barzani may come to Baghdad on Sunday.

KHALILZAD